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SUBJECT: SCENE SETTER: PRESIDENT LULA'S VISIT TO CHINA

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1. (U) Summary: Brazil's President Luis Inacio Lula da Silva visits China May 22 - 27, accompanied by a huge entourage of Ministers and business leaders, determined to put Brazil-China relations at the center of his quest for strategic alliances. Trade and investment may be the most visible items on the agenda, but China figures prominently in the Lula administration's campaign to tighten relations with other like-minded regional heavyweights (i.e., India, South Africa), diversifying its foreign policy alliances and augmenting its own reputation on the world stage. Cooperative activities in science and technology, defense, tourism, environment, and agriculture, invigorated by the higher-profile exchanges within the last year, will likely benefit from a flurry of MOUs and agreements signed during the visit. While the U.S. was Brazil's largest single-country export market in 2003, China came in third, nearly edging out neighbor Argentina, and has been buying even more this year. The GoB seeks deeper trade ties with China, hopes to get its share of China's excess investment capital and would have more to lose from a cooling of China's economy than would many other countries. At the same time, Mercosul and the PRC are discussing the initial phases of a free-trade agreement. While Sino-Brazilian relations, political and commercial, are relatively young, there appears to be no shortage of Brazilian enthusiasm for overcoming the obstacles of inexperience in forging a stronger partnership. The question is whether the PRC shares Brazil's vision of an important strategic relationship, or prefers a marriage of convenience based on short-term interests. End summary.

The Trip of the Century

2. (SBU) President Lula, who visited China once before becoming President, has characterized this trip as perhaps the most important of his government. The sheer size of the delegation supports this assessment. Lula will reportedly bring nine Ministers, at least five governors, and a business delegation of over 400. The trip includes stops in Shanghai and Beijing. In recent remarks to the press, Lula said he wants a "relationship of equals without dependency" with China and, in reference to the bilateral trade relationship, that Brazil needs to do more than just sell. While expectations for greater trade and investment gains are high, the political optic for Brazil is not to be underestimated. Lula views his administration's foreign policy, and perhaps much of his personal legacy, in the context of coalition-building among developing nations. In particular, the GoB considers China a partner in counter-balancing the influence of wealthier nations in multilateral institutions. In the lead-up to the trip, the administration has characterized Brazil and China as nations with much in common.

Common Political Ground?

3. (SBU) Perhaps no other non-western-hemisphere country figures more prominently in the GoB strategic calculus than China. President Lula's visit to Beijing, following high-profile travel to India, South Africa and the Middle East last year, provides ample evidence of the administration's aims to build a formidable bloc of developing countries. A key GoB focus is consensus building among like-minded countries for UN reform that would expand permanent membership of the UN Security Council - presumably to include regional powers such as Brazil. Brazil's Foreign Ministry (MRE) perceives China, already a permanent UNSC member, as sympathetic to this GoB objective. The MRE also believes the two countries share a "political understanding" concerning an emphasis on "multilateralism" and the need to counterbalance U.S. hegemony.

14. (SBU) President Lula's Workers' Party (PT) has also discovered its own "China card." On April 23 in Beijing, PT President Jose Genoino signed a protocol of collaboration between the Chinese Communist Party and the PT. According to press reports, Genoino affirmed that the GoB sought to construct a "diplomatic, political, and economic axis" among India, South Africa, Brazil and China. He praised China's integrated public administration and said it was important for the PT to study what has occurred in China over the last twenty years. Comment: Genoino's visit should not just be viewed as a precursor to the President's upcoming trip. The PT is likely also seeking to score points with Brazil's leftists, including those within the PT itself. End comment.

15. (SBU) During recent UN Commission on Human Rights (UNCHR) meetings in Geneva, Brazil was careful not to favor resolutions critical of China's human rights record, a position criticized by some editorials in the Brazilian press. Brazilian diplomats claim they are not ignorant of the human rights situation in China. The Chief of MRE's Asia and Oceania Division Oswaldo Biato indicated to poloff the GoB perceived China's human rights situation as "serious but improving." In any case, Biato noted, President Lula preferred to deal with this topic directly with his Chinese counterpart. (In a side comment, he said the MRE would welcome any specific human rights information the USG could provide to be placed within the President's brief.) However, other observers doubted very much whether in the swirl of excitement in the Great Hall, Lula would bring up the topic of human rights or whether, if he did, the Chinese would even deign to discuss the matter.

16. (U) Despite Brazil's multi-ethnic makeup, citizens of Chinese descent represent a tiny fraction of Brazil's population, compared, for example, to Brazilians of Japanese ancestry. Illegal immigration and extradition may yet become an issue between the two countries. The majority of the estimated 50,000 Chinese in Brazil, mostly residing in Sao Paulo, are believed to be in-country illegally.

17. (U) The GoB has also identified China as a major source of pirated goods entering the country. To address Brazilian concerns about illegal immigrations and IPR, a legal cooperation agreement will reportedly be discussed during the visit. A Brazilian Congressional investigation of IPR piracy, underway since June 2003, has highlighted the growing influence of the "Chinese mafia" in Sao Paulo's criminal network of contraband and pirated goods peddlers.

18. (SBU) Escola Euro-Americana Professor Ricardo Caichiolo, an expert on Chinese-Brazil relations, bemoaned to poloff the lack of understanding among Brazilians, even among so-called experts, of China. Within the Foreign Ministry, Caichiolo believed that not one official can speak passable Mandarin (Caichiolo himself does not speak Chinese.) Within Brazilian academia, he pointed to a paucity of Chinese Studies programs, although the University of Sao Paulo's and National University of Brasilia's own programs, he commented, were notable exceptions. Academic exchanges are very few, due in part to the strong desire among the youth in both countries to seek English-speaking programs, according to MRE's Biato. However, he expects the development of exchange programs to increase following the visit.

Trade and Investment

19. (U) Despite poor communication, weak historic links, and divergent policy orientations, Brazil and China have recently made significant strides in expanding trade. Commercial linkages which progressed slowly following the first bilateral accord in 1978 have boomed over the last three years. China advanced from 12th place among Brazil's single-country export markets in 2000 to its third largest in 2003, and its expansion continued in the first months of

2004. (Note: The EU, counted as a single market, is Brazil's biggest trading partner, accounting for over U.S. \$30 billion in 2003 trade compared to U.S. \$26 billion with the United States.) Brazil's trade with China in the first trimester of 2004 is already over 25 percent of Brazil's trade with the U.S. during the same period.

110. (U) Note: While Brazil does not recognize Taiwan as a sovereign nation, trade is up approximately 20 percent with the island so far this year; total trade in 2003 was U.S. \$676 million. Brazil's trade data identifies Macao and Hong Kong as separate markets from China, as each has separate customs and tariff arrangements, although politically Brazil recognizes the two territories as falling under Chinese sovereignty. Trade with Hong Kong totaled U.S. \$944 million in 2003; trade with Macao was U.S. \$7 million. Brazilian exports to Hong Kong are up over 30 percent from last year. End note.

111. (U) The PRC is now Brazil's biggest trading partner in Asia, a bilateral relationship worth US \$6.7 billion in 2003

and projected by the GoB to rise to US \$10 billion this year, not including Hong Kong and Macao. Brazil enjoyed a US \$456 million trade surplus with China for the first trimester of 2004, up from US \$330 million during the same period in 2003. Emphasizing the mutual benefits of the growing trade relationship, Minister of Development, Industry, and Foreign Trade, Luis Furlan, confirmed to Chinese and Brazilian business audiences last month that both imports and exports have increased approximately 60 percent in the last trimester over the same period in 2003. China's top exports to Brazil include transmitter parts, electronics, textiles, liquid crystal displays, computers, coal, electric motors and stereo equipment.

¶12. (U) Soybeans, iron ore and steel products accounted for approximately 75 percent of the value of 2003 Brazilian exports to China. China is the largest buyer of Brazilian soy and iron ore, and the second largest importer of Brazilian steel. Other top exports include cellulose and other wood products, laminated iron or steel sheets, leather, and automobile motors and parts. While seeking to export higher value-added, manufactured goods to the Chinese, the GoB recognizes that China's demand for primary products like soy and steel currently drive the relationship. The desire for uninterrupted supply of these primary-product exports will fuel the GoB-estimated US \$5 billion of Chinese investment during the next three years in Brazilian mining, steel, transport infrastructure, energy and agribusiness. The Lula administration has launched an ambitious Public-Private Partnership (PPP) initiative to help improve the country's woefully inadequate infrastructure using mostly private capital (ref A). While the implementing PPP legislation still awaits final Congressional approval, the GoB would like to see PPPs used as the vehicle for some of the hoped-for Chinese investment.

¶13. (U) MRE's Biato told econoff of Chinese interest in further joint venture projects with Companhia Vale do Rio Doce (CVRD), which could duplicate the success of Harbin Aircraft/Hafei Aviation's joint venture with Embraer to build regional jets. CVRD plans to inaugurate a steel mill in the state of Maranhao in the coming months, the result of a Chinese joint venture with Baosteel Group. CVRD is also discussing with Chinese investors exploration of a recently discovered copper mine in the same state. CVRD representatives announced plans to build the world's largest solid cargo transport ship at a trade seminar last month, to deliver iron ore to China. Brazil is a partner in the construction of the world's largest hydropower project at Three Gorges, and recent press reports have speculated on joint ventures in the farming and processing of soybeans as well as exploration of uranium deposits in Brazil.

¶14. (U) Citing economic complementarities between the two countries, MDIC trade promotion officials interpret China's growing energy needs as offering great potential for innovative Brazilian technology -- flex-fuel technology, ethanol production and sales, hydroelectric machinery, as well as deepwater oil and gas sector know-how and equipment. Petrobras and the China National Petroleum Corp. have reportedly held talks on forming an oil exploration venture. The complementarity projections extend to China's need to invest its excess capital and Brazil's cash-starved infrastructure projects as well as the growing Chinese middle class's expected desire for increasing amounts of Brazilian meats, frozen chicken, orange juice, furniture, medical equipment and shoes. The Brazilian Ministry of Agriculture announced in February that Chinese officials had expressed interest in building railways, roads and other infrastructure in exchange for Brazilian soy, cotton and ethanol. While the mechanics of such a barter arrangement would likely present problems for Brazil's private growers, the idea of investing in infrastructure projects linked to transporting commodities persists. The Chinese Ambassador to Brazil recently told participants at a Brazil-China investment conference that China is studying the possibility of investing in road networks through Brazil to Pacific ports.

¶15. (U) In advance of the trip, both GoB and Chinese diplomats here are downplaying the decreased growth expectations of the Chinese economy, despite the significant effect that dampened demand for commodities like soy and iron ore would have on Brazil in particular. Chinese officials prefer to spotlight the 2008 Olympics and the government's promise to raise the median income level and double GDP by 2020, longer-term goals that a temporary economic slowdown will not heavily impact. The Brazilians, in turn, do not appear concerned that the investment they seek might diminish, secure in their belief that Chinese financial authorities acting early will prevent a crisis.

¶16. (U) Since few academics or public servants, let alone business people, are knowledgeable about China, the GoB argues that expanded bilateral trade, tourism, and cultural promotion efforts are the keys to solidifying and expanding mutually enriching exchanges. In the run-up to Lula's visit,

several high-level exchanges of trade and investment missions have laid the ground-work for the official inauguration of the Brazil-China Business Council (CEBC), an entity comprising representatives of China's and Brazil's largest and most successful companies. The CEBC Co-Presidency will be shared between CVRD's President Roger Agnelli and China's Minmetal's President Miao Gengshu. President Lula will inaugurate the CEBC during his visit.

17. (U) In addition to the CEBC being an effective tool of business promotion, the GoB views it as the embodiment of both countries' highest-level dedication to exploiting the other's untapped potential, ending a period of unintended benign neglect. Along with the CEBC's inauguration, two match-making business seminars are slated for the accompanying 400-member business delegation: one in Beijing, the other in Shanghai. While this business delegation is organized by the MRE's Trade Promotion Department, Biato explained that the CEBC will undertake activities across the two countries that official trade promotion agencies are too small and inexperienced to handle.

18. (U) APEX, Brazil's export promotion agency linked to the Ministry of Development, Industry and Foreign Trade, plans a mid-June trade mission to Shanghai focused on sectors identified by a private consultant as having the greatest export potential to China, including specialty coffees, software, cosmetics, gemstones, sports equipment, wine and biotechnology products. A Chinese business delegation from Shanghai Sugar, Cigarettes and Wine plans to visit Brazil next week for meetings with over 50 Brazilian makers of retail items of interest to China's wealthy, a reverse trade mission organized by APEX.

19. (U) In March, Brazilian news outlets reported that China's WTO Ambassador, Sun Zhenyu, had announced the country's desire to explore the possibility of a free trade agreement with Mercosul, as well as with South Africa, Chile, Australia and New Zealand. He highlighted China's ongoing trade agreement discussions with ASEAN and several individual Asia nations. After a visit to Beijing in April, Brazilian Foreign Minister Amorim announced that Mercosul and China would initiate the project of a free trade agreement in May. Mercosul is currently pursuing a wide-ranging FTA with the EU, but has initiated limited preferential trade agreements (PTA) with India and South Africa as precursors to broader future agreements. The agreement with China would also likely start as a PTA focused on gradual tariff reductions for negotiated sets of products of interest to each party. The Lula administration's emphasis on strengthening Mercosul's global reach complements its designs to lead the block of developing nations in the multilateral trade arena. Brazil counts China among the founding members of the G-20 and expects high-level Chinese participation at the June 2004 UNCTAD meeting to be held in Sao Paulo.

Bilateral Cooperation Efforts

20. (SBU) Science and Technology: Brazil's cooperation with China in science and technology fields (ref C) has expanded in recent years, most notably with the China-Brazil Earth Resources Satellite program (CBERS). In October 2003, the second of a series of 4 satellites was launched from a base in northern China. The satellites are equipped with cameras to monitor environmental and natural resource indicators. CBERS has paved the way for partnerships in space research. Further discussions regarding energy cooperation, including renewable and nuclear, are likely during the visit. (Note: Brazil's nuclear program has been the focus of recent attention due to pending issues regarding the Additional Protocol of the NPT and the yet-to-be agreed safeguards at one Brazilian nuclear facility. End note.) In April, the two countries inaugurated a Sino-Brazilian software center in the northeastern Brazilian state of Paraiba. The TecOut center will provide specialized services for the creation and international marketing of software products, including market studies and product adaptations. The visit will likely spawn similar joint initiatives.

21. (SBU) Defense: The Brazilians will explore opportunities to expand mil-mil cooperation. Military contacts indicate that while the military relationship is growing via familiarization visits and training exchanges, military sales between the two countries are unlikely, insisting that defense is not a driving force in the relationship. Defense Minister Viegas visited China in November 2003, but he is not expected to accompany the President on this trip.

22. (U) Tourism: MRE officials portray tourism cooperation as contributing to expanded trade and investment, citing the fact that Chinese tourism is on the rise worldwide, accounting for the third largest number of non-European tourists to visit Europe last year. According to Brazilian press reports, the Chinese government will soon announce a change in its visa policy to encourage more tourism --

Chinese will be able to travel to Brazil without obtaining an exit visa.

Agricultural Trade and Cooperation

123. (U) Minister of Agriculture Rodrigues' visit to China last November and Chinese Vice Agriculture Minister Fan Xiaojian's visit to Brazil that same month produced import certifications for Brazilian beef, phytosanitary protocols, and technical exchanges designed to ease difficulties in certifying the sanitary suitability of a range of agricultural products including citrus, chicken, and pork. Last month President Lula and Chinese Vice Premier Hui Langyu signed a preliminary agricultural commodities accord aimed at eliminating tariff and non-tariff barriers. Despite the professed goodwill, Chinese soy concerns over properly identified biotech varieties and quality issues like excessive humidity, aflatoxin, damaged grains, and impurities continue to occasionally hamper Brazilian soy exports. Only after considerable negotiation did China accept Brazil's export certificates regarding biotech content, as the GoB had not approved the use or safety of biotech soy for its own consumers but expected the Chinese to accept the GoB safety certification based on the claim that the Brazilian variety is the same as those grown in Argentina and the U.S., which have both been accepted by China.

124. (U) While these obstacles may in part mask broader Chinese concerns over food security and an over-reliance on imports, GoB officials expect progress on more binding farm-commodity agreements during the visit. Representatives of the Brazilian meat exporters association, ABIEC, will join the business delegation to China seeking direct sales to mainland China to augment established relationships with importers in Hong Kong. ABIEC's current President is former Agriculture Minister Pratini de Moreas. Cooperation agreements on biotech and fisheries research are under discussion, and there is reportedly Chinese interest in Brazil's booming farmed shrimp industry. (Note: Both Brazil and China, along with four other shrimp exporting nations, are currently the targets of an on-going U.S. anti-dumping investigation.)

Comment: Too Much Hype?

125. (SBU) The number of Chinese high-level visits to Latin America, along with growing trade, suggest that China is not discounting the region as it continues to open its markets and expand its own influence, even if economic growth cools. Brazil, with the region's largest economy and biggest population, figures prominently in that context. There is, however, a lot of ground to cover before achieving the kind of strategic partnership that the GoB envisions. Does China's current administration seek to change the geopolitics of trade with a formula compatible with the GoB's? In a relationship among equals, disagreements are aired, but it seems unlikely that trade irritants, not to mention weightier topics such as democratization and human rights, will figure prominently during this visit. Perhaps social issues affecting both countries, such as HIV/AIDS, social inequalities, and poor income distribution will figure on the agenda. Even if the political bond is immature, there are sufficient financial interests to move the relationship forward and this visit should showcase them. For the Brazilians, even a marriage of convenience (as opposed to commitment) is preferable to a perpetual date.

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